THE FUTURE OF THE GERMAN MARK

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Substantially all the commercial countries of the world are today (December 28, 1918) more or less off the gold monetary basis. International exchange is to a large extent subject to arbitrary regulation—the most effective measure being the inter-governmental loans that have been negotiated between the Allies. To the extent that international exchange is free of such regulation, it may be said to be not on a gold, but on a commodity, basis. The exchanges had not reached the levels that probably would have resulted from a full play of the commodity-basis principle when the war ended. Exchange rates, although one of the most sensitive instruments of trade when the fluctuations are within customary levels, have displayed at times during the last four years a certain immobility and lack of full response to trade conditions that can only be explained by people's habit of thought and trade customs. Gold has retained its place in the people's thought as the ultimate measure of values, even when commodities have been the basis of international payments. And paper money, nominally redeemable in a fixed weight of gold, has in many cases been kept much closer to gold par, both in domestic and in international exchange, than was warranted either by the prospects of gold redemption or by the course of international commodity shipments.

The following table shows the range of exchange fluctuations at New York during the war:

Rates for Bankers Sight Drafts

High	Low	7/27/14	12/24/18
England 556 (Aug. 1, 1914)	4.50 (Sept. 1, 1915)	4.92	4.7580
France 460 (July 30, 1914)	6.07½ (Apr. 13, 1916)	5.14 3/8	5.45½
Italy 490 (July 31, 1914)	9.16 (May 27, 1918)	5.16¼	6.36
Switzerland 3.84 (May 20, 1918)	5.52½ (Mar. 2, 1915)	5.14 3/8	4.80
Holland 51¾ (July 22, 1918)	39 5/16 (Apr. 15, 1915)	40¼	42½
Sweden 47.50 (Nov. 2, 1917)	24.28 (Feb. 24, 1915)	a	29.40
Norway 38.00 (Nov. 2, 1917)	24.23 (Feb. 24, 1915)	a	28.20
Denmark 33½ (Dec. 1, 1917)	24 1/8 (Feb. 24, 1915)	26 7/8	27
Spain 30.75 (Apr. 16, 1918)	18.60 (July 2, 1915)	—*	20.05

* Rates unavailable.

The rapidity with which exchange rates have moved toward normal levels since the end of the war is most remarkable. Be-

tween October 1 and November 18, 1918, we witnessed the following changes:

Country	Oct. 1	Nov. 20	Per cent of Change	Per cent of par
England	4.7655	4.765	— .001049%	97.914%
France	5.46	5.4525	+ .0137%	95.958%
Italy	6.35	6.35	0 - - 0 - -	81.601%
Switzerland	4.69	4.95	— 5.543%	104.673%
Holland	.47	.4225	— 10.1063%	105.099%
Sweden	.32	.2800	+ 12.50%	104.477%
Norway	.2950	.2750	— 6.779%	102.611%
Denmark	.2890	.2680	— 7.266%	100 - - %
Spain	.2225	.2000	+ 10.112%	103.626%

To a large extent sentiment and foresight on the part of international bankers caused the movements in the neutral exchanges, although the immediate prospect of less restricted shipping also played an important part. The Allied countries moved the least —the exchanges there are more or less linked with ours and furthermore are in complete control of their respective governments.

Notwithstanding this rapid progress toward normalization, the prospects are that exchange on a large part of the commercial world will remain upon a commodity basis for some time. The United States and Japan are now, in my opinion, in a position to permit the free movement of gold if it were not for the financial cord that binds them to the Allies. England also should shortly be able to permit the free movement of gold, with France following closely. Resumption on the part of the other Allied countries (excluding Russia and the minor countries) may be somewhat slower, but should present no great problems. This, however, cannot be said of the enemy countries, and the problems presented by their situation range from mere hope to utter despair.

We may ignore the problems of Turkey and Bulgaria—they are practically of no importance to the commercial world—and confine ourselves to those of Austria and Germany. Austria has disintegrated into a number of nations, each of which will undoubtedly assume its share of the prewar debt, but most of which will also undoubtedly refuse to assume any part of the war debt. This will leave the extra burden of the war loans resting upon the German part of Austria and Magyar Hungary. The tremendous expansion in the volume of currency, being based either indirectly or directly upon advances made by the Austro-Hungarian Bank to the government during the war, will fall upon the German and

Magyar remnant of the former empire. The financial future here depends almost entirely upon the political future of these countries. Should Hungary sever her connections with Austria—as seems certain at present—she should assume her share of both the war and prewar debts of Austria-Hungary. Being partners in crime, they should be partners in punishment. Just how Hungary would solve her financial problems is not of much importance to the commercial world, but it is difficult to conceive any measure that could bring her back to a gold basis, within a reasonable length of time, short of a drastic revision of the currency amounting to partial repudiation. German Austria probably will ally herself with Germany proper. Bearing in mind the condition in which she applies for membership in the German family, let us consider the problem of Germany herself.

Germany has today, according to the best information I can gather, gold amounting to almost $548,000,000. But part of this was probably taken from Russia. By the terms of the armistice, the Russian part is to be surrendered at once. Although we are unable to state exactly how much we need to reduce the gold holdings, let us take the statement of the Reichsbank of December 14, 1918, at its face value, and count Germany's gold reserve at $548,000,000. At about the same time, Germany had paper money issues of about $7,200,000,000, including Reichsbank notes of about $4,680,000,000, Darlehnskassenscheine of about $2,400,000,000, and around $100,000,000 of Imperial Treasury notes. The foreign debt of the German government is, apparently, small, and much more than offset by credits granted to allies during the war, some of which may some day be collectible. But the domestic funded debt is about $23,500,000,000. In addition, there is a large floating debt, and there are heavy debts incurred by the various states of the Empire, and by the municipalities during the war. Not all of these public debts are to be counted as additional to the paper money outstanding, since to a large extent the paper money is secured by these debts. But with all possible subtractions, the liabilities resting directly or indirectly on the German Empire are appalling, without any consideration of the indemnities sure to be imposed.

The real difficulties of the situation are perhaps more precisely revealed if we consider the enormous expansion of the demand liabilities of the German banks, including the Darlehnskassen, and taking account of both notes and deposits. The full story is hard

to get. But the figures that follow indicate clearly enough the trend.

The Reichsbank notes were only $692,000,000 on July 31, 1914, but reached $4,000,000,000 by October 31, 1918. Deposits in the Reichsbank were $300,000,000 on the earlier date, but had reached well over $2,000,000,000 by the later date, making a total expansion of demand liabilities of over $4,000,000,000. The whole of the $2,400,000,000 of the Darlehnskassenscheine represents war expansion. In addition, we have gigantic swelling of deposit liabilities of the other German banks. Thus, the Deutsche Bank's deposits were $395,000,000 at the end of 1913, and $1,415,000,000 at the end of 1917; the Dresdner Bank (same dates) increased deposits from $240,000,000 to $730,000,000, and the Discontogesellschaft from $250,000,000 to $725,000,000. These increases are partially due to amalgamations. To sum up these items would be misleading, because, on the one hand, there are some duplications—deposits and notes of the Reichsbank are in part assets of the other German banks; and misleading on the other hand, because we have not included in our figures notes of the other German banks of issue, or (much more important) the great increase in deposits of other German banks. But these figures indicate an enormous increase in the current liabilities of German banks.

To offset these, there is little increase in really liquid assets. The great bulk of this expansion must rest on the war obligations of the German government. Commercial and industrial paper of a satisfactory character must be exceedingly scarce. The gold of the Reichsbank increased from $298,000,000 to $607,000,000 between July 31, 1914, and October 31, 1918, but part of this increase has doubtless been drawn from the other banks in Germany and much of it from the pockets of the German people, so that it does not represent net gain for the system as a whole. In any case, it is far from an adequate offset to the loss of liquidity in the great bulk of the assets of the German banks.

The exchange value of the mark, measured through the medium of neutral exchanges according to latest information obtainable (Nov. 18, 1918), is about 58 per cent of par. If the barriers upon trade and exchange operations were to be lifted today, the mark would probably decline further, as Germany would seek to import far more than she could export, and foreign capital would for some time not be likely to flow there. Admitting the German

part of Austria will certainly not lessen her financial problems. On the contrary, they would be greatly increased thereby. The indemnities exacted by the Allies will add to her external obligations that must ultimately be paid by exports of commodities or gold. All these factors show the extremely difficult position in which Germany will find herself when she seeks to reënter the world's markets. She cannot enter with her currency on any other than a commodity basis in international exchange, and if she decides upon the policy of resuming the gold basis by means of contraction of currency through taxation and the funding of loans, the operation will require many years. A vigorous policy by a strong government could contract the outstanding paper to a point that would permit resumption of gold payments. The process would be to collect the hoarded paper money from the people by taxation or public loans, and turn over the proceeds to the Reichsbank or the Darlehnskassen in cancellation of the government's debts held by these institutions. It is not at all necessary to collect a vast amount of gold before resuming specie payments. But Germany is wholly unlikely to use such a vigorous policy. In the most favorable event which it is reasonable to expect, she would be for many years upon a most unstable basis. Meanwhile, the majority of the commercial world would be operating upon the gold basis, and the mark would be subject to violent exchange fluctuations.

Will Germany adopt this extremely difficult policy, or will she remedy her currency problems and those of German Austria by that favorite nostrum of the politician financier—a revision of the currency? So many well-sounding arguments can be marshalled in favor of the latter that I am inclined to the opinion that some such measure will be attempted. It will be contended that, the government having borrowed a depreciated currency, the debt should not be repaid in a money possessing greater commodity value. It is true that prewar creditors would fare unjustly, but after all the volume of such debts is not to be compared with the volume of the war debt and the currency issues. Furthermore, a revision plan is so easily placed in operation that it presents a tempting avenue of escape for the political financier from the difficult prospect of redeeming debts in gold. A new currency would be issued, into which the old issue of German marks and Austrian crowns would be convertible at par, the gold content of the coin in which the new currency would be redeemable being based upon

international exchange rates of the old mark at the time of the "revision" (or repudiation). Thus the country would immediately find itself "upon a gold basis."

Whether the Allies would permit such a measure is a question that depends upon many factors now uncertain, but at present it does not seem to me that they would be greatly interested. Their indemnities would be payable in gold or its equivalent and they may reason that a "revision" process is less likely to repress industrial activity in Germany than heavy taxation and a contraction of currency. They may, therefore, view with favor such a policy, believing it to add to Germany's ability to pay the indemnities.